REPORT OF THE

FINANCIAL EXAMINATION OF

CHILDREN'S MERCY'S FAMILY HEALTH PARTNERS, INC.

AS OF

DECEMBER 31, 2003

STATE OF MISSOURI

DEPARTMENT OF INSURANCE

JEFFERSON CITY, MISSOURI

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Kansas City, Missouri
August 27, 2004

Honorable Alfred W. Gross, Commissioner
Virginia Bureau of Insurance
Chairman of Financial Condition (EX4) Subcommittee
Southeastern Zone Secretary

Honorable Jorge Gomez, Commissioner
Wisconsin Department of Insurance
Midwestern Zone Secretary

Honorable Scott B. Lakin, Director
Missouri Department of Insurance
301 West High Street, Room 530
Jefferson City, Missouri 65102-0690

Gentlemen:

In accordance with your financial examination warrant, a full scope association financial examination has been made of the records, affairs and financial condition of

Children's Mercy's Family Health Partners, Inc.

hereinafter referred to as Family Health Partners, or as the Company. Its administrative office is located at 215 West Pershing, Kansas City, Missouri 64108, telephone number 816-855-1870. This examination began on June 7, 2004, and concluded on the above date.

SCOPE OF EXAMINATION

<u>Period Covered</u>

The prior full scope financial examination of Family Health Partners was made as of December 31, 2000, and was conducted by examiners from the State of Missouri representing the Midwestern Zone of the National Association of Insurance Commissioners (NAIC).

The current full scope financial examination covers the period from January 1, 2001, through December 31, 2003, and was also conducted by examiners from the State of Missouri representing the Midwestern Zone of the NAIC with no other zones participating.

This examination also included the material transactions and/or events occurring subsequent to the examination date which are noted in this report.

Procedures

This examination was conducted using the guidelines set forth in the Financial Condition Examiners Handbook of the NAIC, except where practices, procedures and applicable regulations of the Missouri Department of Insurance and statutes of the State of Missouri prevailed.

The examiners relied upon internal control narratives and internal control testing supplied by the Company's independent auditor, KPMG, LLP, of Kansas City, Missouri, for its audit covering the period from January 1, 2002, through December 31, 2003.

Comments - Previous Examination

Listed below are the comments, recommendations, and notes from the previous examination report, the Company's response, and the findings in the current examination.

Form B Filing

Comment: The 2000 Insurance Holding Company Annual Registration Statement (Form B) was not properly completed. The Third Party Administrative Services Agreement with Truman Medical Center (TMC) was not disclosed as required, the Form B filing incorrectly identified two agreements with Children's Mercy Hospital (CMH) that were actually with Children's Mercy Health Network (CMHN) and CMHN was incorrectly omitted from the organizational chart. The Company was directed to ensure these errors and omissions were corrected for future Form B filings.

Company's Response: The Company will properly reflect the agreements with CMHN in future Form B filings. The Third Party Administrative Services Agreement with TMC has been terminated.

Current Findings: The Insurance Holding Company Annual Registration Statements filed during the examination period were reviewed. The only significant error or omission noted was that the Asthma Grant Agreement with CMH was not properly disclosed. See the Intercompany Transactions section of this report for recommendations.

Joint Operating Agreement

Comment: The administrative percentage of premiums retained by the Company was changed from 10% to 8% in September 2000 and from 8% to 9% in January 2001 without any type of formal written agreement. The Company was directed to execute written agreements for these and all future changes to the administrative percentage.

Company Response: Changes to the administrative allocation were required to be in writing per the Joint Operating Agreement in effect at the time of the prior examination. However, the Joint Operating Agreement was terminated as of January 31, 2002, and therefore, is irrelevant to future transactions.

Current Findings: The prior comment no longer applies due to the termination of the Joint Operating Agreement.

Joint Operating Agreement

Comment: Payments were not made between the Company, CMH and TMC to settle year-end risk pool balances, in accordance with the Joint Operating Agreement. The risk pool balances were improperly maintained as continuous rolling balances. The agreement requires that payments be made between the parties by August 1 of each year to settle the December 31 risk pool balances of the prior year. The Company was directed to properly settle the year-end risk pool balances by the dates specified in the Joint Operating Agreement.

Company's Response: The risk pool balances reported are merely estimates based on incurred but not reported claims. The Company billed and received payment in full for the receivable risk pool balance from TMC in October 2002, and the Company released payment due to CMH periodically throughout the year. The Company believes that a periodic payment schedule is not in conflict with the terms of the Joint Operating Agreement. In future periods, the Company intends to word any inter-company agreements of this nature to properly reflect the subsequent actuarial reviews, re-assessments and adjustments necessary for final determination of risk pool balances.

Current Findings: The prior comment no longer applies due to the termination of the Joint Operating Agreement and subsequent settlement of the risk pools.

Reliastar Reinsurance Agreement

Comment: The Company was directed to revise the terms of the reinsurance agreement with Reliastar Life Insurance Company, as requested in the August 6, 2001 letter from the Missouri Department of Insurance (MDI).

Company's Response: The Company accepted the need to revise the reinsurance agreement as requested by the MDI, and made efforts to do so with the reinsurer. However, the agreement in question was terminated before a revised agreement could be obtained.

Current Findings: The Company's reinsurance agreement with Reliastar Life was terminated effective December 31, 2001. The subsequent reinsurance agreements the Company entered into were reviewed and no significant problems were noted.

Third Party Administrative Services Agreement

Comment: The Company did not file the Third Party Administrative Agreement (TPA) with TMC for prior approval by the MDI as required by Section 382.195 RSMo. (Transactions Within a Holding Company System). The Company was directed to immediately submit a Form D filing for this agreement.

Company's Response: The Company terminated TPA services with TMC effective December 31, 2001.

Current Findings: TMC is no longer a member of the Company's holding company system. In addition, the Company has terminated its TPA agreement with TMC and surrendered its TPA license.

Paid Claims Data

Comment: The Company could not locate 13% of paid claims from its archived information maintained on microfiche and CD-ROM's, for a sample requested during the examination. It was recommended the Company review its procedures for archiving claim information submitted by providers and implement new procedures to ensure claims are properly archived in the future.

Company's Response: The Company reviewed its procedures for archiving claims and made necessary improvements.

Current Findings: No problems were noted in the current examination relating to the retention of claims information.

HISTORY

General

The Company was organized as a not-for-profit corporation under the Missouri Non-Profit Corporation Law (Chapter 355 RSMo), on July 11, 1995, under the name "TruCare, Inc." At the incorporation date, the sole owner of the Company was Truman Medical Center, Inc. The name of the Company was changed to "TrumanCare, Inc." on December 20, 1995. Subsequently, Children's Mercy Hospital became a 50% owner of the Company and, the name was changed again on March 26, 1996, to Children's Mercy Hospital/Truman Medical Center dba Family Health Partners, Inc. A Certificate of Authority to operate as a Health Maintenance Organization under Chapter 354 RSMo (Health Services Corporations – Health Maintenance Organizations – Prepaid Dental Plans), was issued by the MDI on May 6, 1996. Effective February 1, 2002, TMC withdrew as part owner of the Company leaving CMH as the sole remaining owner. The Company's name was then changed to Children's Mercy's Family Health Partners, Inc. to reflect the new ownership.

Capital Stock

Family Health Partners does not have any capital stock ownership because of its organization as a not-for-profit corporation. The ownership interest of CMH in Family Health Partners is authorized in the Company's Articles of Incorporation.

Dividends

No dividends or cash distributions were made or declared during the examination period.

Management

The management of the Company is vested in a Board of Directors that is appointed by the sole owner, Children's Mercy Hospital. The Bylaws in effect when the 2003 Board of Directors were appointed specified that the Board of Directors should consist of eight voting members. In addition, three non-voting members could be appointed. The Board of Directors appointed and serving as of December 31, 2003, were as follows:

Name and Address	Principal Occupation and Business Affiliation
Voting Members	
Randall O'Donnell, Chairman Leawood, KS	President and Chief Executive Officer, CMH
Jo Stueve, President Kansas City, MO	Vice President Managed Care, CMH
Dwight Hyde, Secretary/Treasurer Overland Park, KS	Senior Vice President and CFO, CMH
Robert Long Leawood, KS	Vice Chairman, J.E. Dunn Construction Company
Robert Cross Mission Hills, KS	Executive, The Cross Foundation
V. Fred Burry, M.D. Kansas City, MO	Executive Medical Director, CMH
David Oliver Kansas City, MO	Partner, Berkowitz, Feldman, Stanton, Williams & Stueve
Leland McGinness Kansas City, MO	Administrative Chief of Staff, CMH
Non-Voting Members	
Lloyd Olson, M.D. Parkville, MO	Pediatrician-in-Chief, CHM
Robert Finuf Lenexa, KS	Chief Executive Officer, Family Health Partners

Ben Rubin, Jr. M.D. Leawood, KS	Associate Medical Director, CMHN

Effective February 17, 2004, the composition of the Board of Directors was changed to allow for more community representation, and to increase the number of voting directors to nine in accordance with revisions to the Bylaws. Robert Long and David Oliver were replaced by other individuals not employed by Family Health Partners or CMH. Dwight Hyde and V. Fred Burry were made non-voting members, and Mr. Hyde was replaced by Leland McGinness as Secretary/Treasurer. Five new directors were appointed as follows:

Name and Address	Principal Occupation and Business Affiliation
Voting Members	
John Borden Leawood, KS	Executive Consultant, Central Baptist Theological Seminary
B. Spencer Heddens Shawnee Mission, KS	Senior Vice President, Bank of America
John Ovel Mission Hills, KS	Trust Division Manager, Commerce Bank
John Wood Kansas City, MO	Mortgage Bank Manager, Wells Fargo
Robert Welling Warrensburg, MO	Self Employed Attorney

Senior management employed to manage the day-to-day operations of Family Health Partners as of December 31, 2003, were as follows:

Chief Executive Officer	Robert Finuf
Director of Finance	B. Suzie Dunaway
Director of Health Services	Ma’ata Touslee
Director of Operations	Linda Steinke
Director of Community and Government Relations	Taira Green
Director of IT/IS	Christine Harrington
Compliance Officer	Mikki Massey

The Bylaws do not specify any named committees of the Board of Directors. However, the Company's Bylaws provide for the Board of Directors to establish, as needed, committees which shall have the authority of the Board of Directors. Such committees must consist of at least three voting directors and may also include other individuals. As of December 31, 2003, there were no committees established having the authority of the Board of Directors.

The Bylaws also provide that the Board of Directors may designate committees which do not have the authority of the Board of Directors. These committees are not formal committees of the Board of Directors, and are utilized primarily to aid management. The Board of Directors does not elect any of the members of these committees. The committees designated as of December 31, 2003, were as follows:

Medical Oversight	Administrative Oversight
Medical Management	Health Plan Outreach
Credentialing Committee	Transportation
Pharmacy & Therapeutics	

Conflict of Interest

The Company has procedures that require all officers and directors to complete a conflict of interest statement each year. Signed conflict of interest statements were reviewed for the examination period, and no significant conflicts were disclosed.

Corporate Records

The Articles of Incorporation and Bylaws were reviewed. Both the Articles of Incorporation and Bylaws were amended and restated on February 1, 2002, to reflect the change in ownership of the Company. The Bylaws were amended and restated again on December 9, 2003, to require greater community representation on the Board of Directors pursuant to a determination by the Internal Revenue Service of the Company's tax-exempt status.

The Board of Directors' meeting minutes, Annual Member meeting minutes, and the Committee meeting minutes were reviewed for the examination period and subsequent periods. The meeting minutes, in general, appear to properly reflect and approve the Company's transactions and events for the period under examination.

Acquisitions, Mergers and Major Corporate Events

Pursuant to a Termination and Withdrawal Agreement effective February 1, 2002, Truman Medical Center withdrew as part owner of Family Health Partners. Under the Joint Operating Agreement (JOA) in effect between Family Health Partners, CMH and TMC prior to the withdrawal, TMC and CMH had been responsible to ensure that Family Health Partners maintained sufficient capital reserves and surplus. This was accomplished through the establishment of separate risk pools. TMC was responsible for the MC+ Adult Risk Pool and CMH was responsible for the MC+ Pediatric Risk Pool. The Termination and Withdrawal Agreement terminated the JOA and various administrative service agreements between Family Health Partners and TMC. The risk pools were dissolved and a final settlement of the MC+ Adult Risk Pool was made with a $138,007 payment from TMC to Family Health Partners in July of 2002. CMH was paid a total of $3,375,034 in 2002 and received a final payment of $414,377 in March 2003 as settlement of the Pediatric Risk Pool.

In addition to the settlement of the risk pools, the Termination and Withdrawal Agreement required CMH to make an unrestricted charitable contribution to TMC equivalent to 50% of the value of Family Health Partners as reflected in the December 31, 2001 audited financial statements. This charitable contribution was intended to reimburse TMC for its capital contributions made to support Family Health Partners. The charitable contribution was paid in full by CMH in 2002 with total payments to TMC in the amount of $1,636,640.

Surplus Debentures

No surplus debentures were issued or outstanding for the period under examination.

AFFILIATED COMPANIES

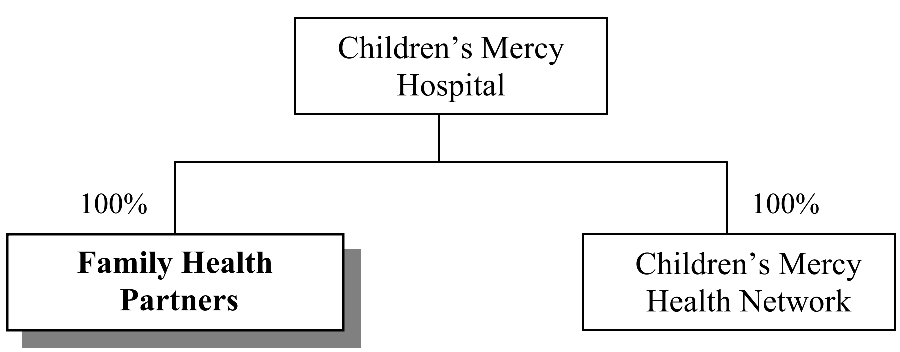
Holding Company, Subsidiaries and Affiliates

The Company was owned 50% by Truman Medical Center and 50% by Children's Mercy Hospital. Effective February 1, 2002, TMC sold its entire interest in Family Health Partners to CMH, and Family Health Partners became solely owned by CMH.

Children's Mercy Hospital is a not-for-profit teaching hospital for children located in Kansas City, Missouri. CMH is a holding company as defined by RSMo 382.010 (Definitions). Besides Family Health Partners, the CMH holding company system includes Children's Mercy Health Network (CMHN) which is a corporation formed for the purpose of contracting and administering the managed care contracts of CMH.

Organizational Chart

The following organizational chart depicts Family Health Partner's ownership and holding company system, as of December 31, 2003:



Intercompany Transactions

The Company's significant intercompany agreements as of December 31, 2003, are outlined below.

1. **Type:** Administrative Service Agreement for Personnel and General Services

   Affiliate: Children's Mercy Hospital

   Effective: April 1, 1996; revised and restated June 1, 1999, restated February 1, 2002

   Terms: CMH will provide personnel for the operation of Family Health Partners. The employees shall remain employees of CMH, and salaries of the employees will be determined upon mutual agreement of the parties. Family Health Partners will reimburse CMH, on a monthly basis, for 119% of the salaries of the applicable employees. The 19% add-on represents compensation for the cost of employee benefits. Family Health Partners will also reimburse CMH for recruitment and food service costs of employees.

2. **Type:** Participating Provider Agreement

   Affiliate: Children's Mercy Health Network

   Effective: January 1, 1997; revised and restated June 1, 1999, restated February 1, 2002.

   Terms: CMHN shall arrange for the provision of hospital and medical services for the members of Family Health Partners. For each medically necessary inpatient day, Family Health Partners will compensate CMHN $1,758. All outpatient hospital services, ancillary services, and physician services performed by employed and contracted physicians of CMH who are Family Health Partners participating providers will be capitated. CMHN will receive a capitation payment from Family Health Partners for its services to subscribers, other than inpatient services, based on an estimate of payments for all services to non-CMH providers. Should the capitation need to be adjusted due to an inaccurate estimated payment to non-CMH providers, Family Health Partners will adjust its capitation payment to CMH to assure adequate reserves.

3. **Type:** Administrative Services Agreement for Nurse Advice Services

   Affiliate: Children's Mercy Hospital

   Effective: January 1, 1997; revised and restated June 1, 1999; restated February 1, 2002

   Terms: CMH will establish and maintain a telephone system, which will allow the members of Family Health Partners to call nurse advisors with questions regarding medical care. The phone line will be available 24 hours a day, 7 days a week. Family Health Partners will pay CMH $0.53 per member per month for each member.

Exception: The Company calculates the compensation amount due to CMH based only on pediatric members. However, the agreement itself does not make a distinction between pediatric and adult members. Therefore, it appears the calculation should include both pediatric and adult members. Since Family Health Partners still pays TMC for nurse advise for adult members and CMH only provides nurse advice to pediatric members, it appears that there is an understanding between the parties that CMH will only be compensated for pediatric members. However, the Company should amend the Administrative Service Agreement for Nurse Advice Services so that it reflects the intent of the parties.

4. **Type:** Administrative Services Agreement for Medical Director Services

   Affiliate: Children's Mercy Health Network

   Effective: January 1, 1997; revised and restated on June 1, 1999; restated February 1, 2002

   Terms: CMHN will employ or contract for a medical director(s) to provide services for Family Health Partners. Family Health Partners will pay $12,500 per month to CMHN for these services.

5. **Type:** Guaranty Agreement

   Affiliate: Children's Mercy Hospital

   Effective: February 1, 2002

   Terms: CMH shall be responsible for ensuring that Family Health Partners maintains the necessary capital reserves and surplus as necessary to support the HMO products offered by the Company. CMH shall review the financial condition of Family Health Partners on a monthly basis and make necessary capital contributions upon approval of CMH's Board of Directors to cover the losses of Family Health Partners.

   Exception: The Company failed to file the Guaranty Agreement with the MDI for prior approval as required by Section 382.195, RSMo (Transactions Within a Holding Company System). The Company is directed to submit a Form D filing for this agreement.

6. **Type:** Asthma Grant Agreement

   Affiliate: Children's Mercy Hospital

Effective: October 15, 2001

Terms: Family Health Partners received a grant from the Robert Wood Johnson Foundation to provide asthma education and testing services to plan members. The term of the grant is from October 12, 2001 through October 14, 2004. CMH is to provide the employees and facilities necessary for the administration of the grant. Family Health Partners will reimburse CMH not more than monthly for costs incurred.

Exception: The Company failed to file the agreement with the MDI for prior approval as required by Section 382.195, RSMo (Transactions Within a Holding Company System). In addition, the Company failed to disclose the agreement separately on its Insurance Holding Company System Annual Registration Statement filing with the MDI. The Company is directed to ensure that any future agreements of this type are properly filed with the MDI and properly disclosed.

The amounts paid to and received from the parent, affiliates and subsidiaries during the period under examination under the above agreements were as follows:

	2003	2002	2001
Administrative Service Agreement for Personnel and General Services:			
Paid to Children's Mercy Hospital	(4,183,627)	(3,505,148)	(1,712,151)
Participating Provider Agreement:			
Paid to Children's Mercy Health Network	(21,646,817)	(17,855,944)	(9,879,229)
Administrative Service Agreement for Nurse Advice Services:			
Paid to Children's Mercy Hospital	(228,136)	(213,532)	(232,762)
Administrative Agreement for Medical Director Services:			
Paid to Children's Mercy Health Network	(150,000)	(131,250)	(75,000)
Guaranty Agreement:			
Paid to Children's Mercy Hospital	-0-	-0-	-0-
Asthma Grant			
Paid to Family Health Partners	(363,197)	(222,233)	-0-
Net Amount (Paid) or Received	**$(26,571,777)**	**$(21,928,107)**	**$(11,899,142)**

In addition to the above agreements, during the examination period, the Company was a party to various agreements with Truman Medical Center prior to its withdrawal as an owner effective February 1, 2002. The terms of these agreements and payments made are not included in this report since TMC was no longer an affiliated party as of December 31, 2003.

FIDELITY BOND AND OTHER INSURANCE

The Company is a named insured on a crime insurance policy maintained by its parent, Children's Mercy Hospital. The policy provides fidelity coverage with a liability limit of $3,000,000 and a $10,000 deductible. This level of fidelity coverage complies with the suggested minimum amount of insurance according to NAIC guidelines and Section 354.425, RSMo (Surety Bond Requirements).

The Company is also a named insured on other standard types of coverages which include, but are not limited to: directors and officers liability, property and excess liability, commercial general liability, managed care organization errors and omissions, commercial general liability, and workers compensation. These additional insurance coverages appear adequate.

PENSION, STOCK OWNERSHIP AND INSURANCE PLANS

Family Health Partners does not have any direct employees. The Company's business operations are performed by employees of its parent, Children's Mercy Hospital, in accordance with the provisions of an Administrative Services Agreement that is explained in greater detail in the Intercompany Transactions section of this report.

The CMH employees receive standard benefits, which include but are not limited to, paid vacation and sick leave, educational assistance, medical and dental insurance, life insurance, long-term disability benefits, tax deferred annuities, flexible spending accounts and a defined contribution retirement plan.

The Company appears to have properly accounted for its liabilities for employee benefits.

STATUTORY DEPOSITS

Deposits with the State of Missouri

The funds on deposit with the Missouri Department of Insurance as of December 31, 2003, as reflected below, were sufficient to meet the capital deposit requirements for the State of Missouri in accordance with 354.410 RSMo (Trust Deposits and Capital Requirements). The funds on deposit were as follows:

Type of Security	Par Value	Fair Value	Statement Value
U.S. Treasury Bill and Notes	$1,702,000	$1,709,978	$1,712,401

Deposits with Other States

The Company does not maintain funds on deposit with any other state.

INSURANCE PRODUCTS AND RELATED PRACTICES

Territory and Plan of Operation

Family Health Partners is licensed in the state of Missouri under Chapter 354 RSMo, as it relates to Health Maintenance Organizations. The service territory, as of December 31, 2003, was concentrated in 9 counties in western Missouri. The Company's only product is Medicaid managed care. The Company has applied for and has been awarded contracts by the State of Missouri Division of Medical Services (DMS) to provide managed care services to Medicaid recipients in Missouri. The latest contract awarded to the Company was for a one-year term starting January 1, 2004 with two additional one-year renewal periods at the sole option of DMS. The Company had 49,328 members as of December 31, 2003, enrolled through the Missouri MC+ Program.

The Company is also licensed in the State of Kansas; however, the Company's contract with the State of Kansas to provide Medicaid Services expired July 1, 2001, and was not renewed. Therefore, the Company currently has no Kansas members.

Marketing

The Company obtains members one of two ways, either a Medicaid eligible individual will select Family Health Partners over its competitors, or members will be automatically assigned to Family Health Partners by DMS. The Company's marketing activity is primarily focused on attending festivals, community outreach programs, newsletters, publications and distributing pamphlets containing information about its products. The community outreach programs include school education programs, seminars for providers to educate about disease preventative measures and programs held by the Company's owner hospital. The Company has a Director of Community and Government Relations, a Manager of Community Relations and two Community Relation Representatives who coordinate the marketing and community outreach activities. The Company does not utilize any brokers or agents and does not have any direct solicitation for membership, as required by the Medicaid contract with the State of Missouri.

Provider Contracts

The Company has provider contracts with primary care physicians, specialists, ancillary providers and hospitals. Primary care physician services are compensated at 110% of the Missouri Medicaid rate. Specialist and ancillary providers are compensated at 100% of the Missouri Medicaid rate or on a case by case basis. Hospital rates are based upon negotiated per diem rates, percentage of discounts from billed charges or fee for service rates.

The Company subcontracts through provider agreements, to a dental managed care services organization and to a behavioral managed care organization, for all dental and mental health care services for members. A per member per month capitation fee is paid for these services.

The Company subcontracts with AdvancePCS Health, L.P., a licensed TPA in the State of Missouri, for the management of prescription drug benefits to include providing a network of retail pharmacies, mail service, claims processing, customer service, formulary services and drug utilization reviews.

Rates

Premium rates throughout the exam period were established through a bid and negotiation process with the State of Missouri, which were subject to maximum levels as determined by the State. Beginning with the January 1, 2004 contract, premium rates are subject to actuarial soundness testing per guidance provided by DMS and are no longer subject to maximum levels. Members are separated into age and sex based categories with varying premium amounts for each category. The Company receives a supplemental, lump-sum premium for each live birth delivery to a member. All premiums due to Family Health Partners are paid entirely by the State of Missouri on behalf of the members.

Grievance Procedures

The Company distributes a Member Handbook to each member, which describes the procedures for complaints, grievances, and appeals. Members have the option of submitting complaints to Family Health Partners, DMS, or both. The Company maintains a register to monitor the status of pending complaints. The Company's Medical Management Committee also discusses and addresses member complaints and service issues.

Quality Assurance, Utilization Review, and Provider Credentialing

The Company is not accredited by the National Committee for Quality Assurance (NCQA). The Company does not plan to seek NCQA accreditation because of its small size and specialization as a Medicaid only HMO. However, the Company does follow the NCQA's guidelines for quality assurance, utilization, and credentialing. The Company's policies and plans are reviewed and approved annually by the State of Missouri.

The Company has a Quality Management (QM) Plan to monitor, evaluate, and improve the quality, accessibility and availability of the health care services that are provided to members. The QM plan includes policies and procedures for the review of data collected from peer reviews, utilization data, medical records, member satisfaction surveys, and other quality of service areas. A Medical Oversight Committee meets to discuss all quality of service issues.

The Company has a Utilization Management (UM) Plan to monitor and evaluate the specific health care provided to members. The UM Plan includes procedures for monitoring referrals, prior authorizations, hospital admissions, case management, discharge planning, and other procedures relative to the management of the medical services received by members. Monthly utilization summaries are prepared to monitor the hospital admissions and length of stays. A Pharmacy and Therapeutics Subcommittee monitors prescription drug utilization and a Medical Management Subcommittee reviews the medical status and care plans for significant claims in progress.

The Company has established policies and procedures for credentialing and recredentialing of providers. Recredentialing reviews are scheduled for every three years. For some providers, the Company relies on the credentialing procedures performed by CMH or other organizations which meet the requirements of the NCQA. Providers must be approved by the Company's Board of Directors subsequent to credentialing and recredentialing reviews in order to participate in Family Health Partner's network.

REINSURANCE

General

The Company's premium activity on a direct written, assumed and ceded basis, for the period under examination, is detailed below:

	2003	2002	2001
Direct Business	$ 87,389,399	$ 81,848,023	$ 72,456,266
Reinsurance Assumed:	-0-	-0-	-0-
Reinsurance Ceded:			
Affiliates	-0-	-0-	-0-
Non-affiliates	(247,925)	(230,821)	(562,765)
Net Premiums Written	$ 87,141,474	$ 81,617,202	$ 71,893,501

Assumed

The Company does not assume any business.

Ceded

The Company is contingently liable for all reinsurance losses ceded to others. This contingent liability would become an actual liability in the event that an assuming reinsurer fails to perform its obligations under the reinsurance agreement.

The Company has a reinsurance agreement with Munich American Reassurance Company. The original agreement was effective January 1, 2002, and has been renewed on an annual basis. Pursuant to the agreement, the Company cedes 80% of its Medicaid inpatient claims subject to a retention of $125,000. The reinsurer's maximum liability is limited to

$1,000,000 per covered member per agreement term. The reinsurance premium rate is $0.43 per member per month.

ACCOUNTS AND RECORDS

Independent Auditor

The Company's financial statements for the years ending December 31, 2003 and December 31, 2002 were audited by the CPA firm of KPMG, LLC, of Kansas City, Missouri. The Company's financial statements for the year ended December 2001 were audited by the CPA firm of Deloitte & Touche, LLP, of Kansas City, Missouri.

Independent Actuary

Claims payable reserves at December 31, 2003, were certified by Clark Slipher, MAAA of Milliman, USA, Inc. in Brookfield, Wisconsin. The claims payable reserves at December 31, 2002 and December 31, 2001, were reviewed and certified by David O. Thoen, FSA, MAAA, of Deloitte & Touche, LLP, of Minneapolis, Minnesota.

Based on its 2004 budget estimates, the Company determined that it did not need to accrue a premium deficiency reserve for 2004 on the December 31, 2003 Annual Statement. The Company's certifying actuary did not include the premium deficiency reserve in his certified actuarial opinion, and therefore, did not opine on whether the Company's decision not to report a premium deficiency reserve was proper or reasonable. The Company's management should ensure that the certifying actuary opines on the premium deficiency reserve in future opinions even if the premium deficiency reserve is determined to be zero.

Custodial Agreements

During our review of the Company's cash and investment accounts, it was noted that the Company's custodial agreements with Bank of America and Central Bank did not contain all of the safeguard provisions specified in Part 1, Section IV of the NAIC Financial Condition Examiners Handbook. The Company should amend or restate its custodial agreements so that they contain all of the NAIC specified safeguard provisions.

FINANCIAL STATEMENTS

The following financial statements, with supporting exhibits, present the financial condition of Family Health Partners for the period ending December 31, 2003. Any examination adjustments to the amounts reported in the financial statements and/or comments regarding such are made in the "Notes to the Financial Statements." The failure of any column of numbers to add to its respective total is due to rounding or truncation.

There were additional differences found in the course of the examination that are not shown in the "Notes to the Financial Statements". These differences were determined to be immaterial concerning their effect on the financial statements when evaluated on an individual basis. The additional differences were communicated to the Company and should be addressed by management. Appropriate action should be taken to resolve the underlying problems, which led to the examination differences.

Assets
as of December 31, 2003

	Assets	Non Admitted Assets	Net Admitted Assets
Bonds	$ 1,925,401		$ 1,925,401
Cash and short-term investments	4,544,310		4,544,310
Investment income receivables	17,409		17,409
Uncollected premiums and agent's balances	7,973,433		7,973,433
EDP equipment and software	417,586	$ 193,494	224,092
Furniture and equipment	132,927	66,464	66,463
Health care and other amounts receivable	59,188		59,188
Other non-admitted assets			
Leasehold improvements	21,445	21,445	-0-
Aggregate write-ins for other than invested assets:			
Asthma grant receivable	96,081		96,081
Prepaid expenses	181,830	181,830	-0-
Total Assets	**$15,369,610**	**$463,233**	**$14,906,377**

Liabilities and Net Worth
as of December 31, 2003

Claims unpaid	$ 10,436,798
Unpaid claims adjustment expenses	134,794
General expenses due and accrued	398,302
Amounts due to parent, subsidiaries and affiliates	594,949
Aggregate write-ins for other liabilities:	
Liability for uncashed checks	53,715
Total Liabilities	**$11,618,558**
Contributed Capital	4,605,000
Unassigned funds	(1,317,181)
Total Capital and Surplus	**$ 3,287,819**
Total Liabilities and Surplus	**$14,906,377**

Statement of Revenue and Expenses
For the Year Ended December 31, 2003

Member Months	**578,106**
Net premium income	$87,141,474
Aggregate write-ins for other health related revenues:	
Grant revenue	191,668
Total Revenues	**$87,333,142**
Medical and Hospital:	
Hospital/medical benefits	$50,512,149
Other professional services	6,807,949
Emergency room and out-of-area	8,986,375
Prescription drugs	13,848,800
Aggregate write-ins for other expenses:	
Transportation expense	482,796
Total medical and hospital expense	**$80,638,069**
Claims adjustment expense	2,808,585
General administrative expenses	4,337,868
Premium deficiency reserve adjustment	(1,129,602)
Total Underwriting Deductions	**86,654,920**
Net Underwriting Gain or (Loss)	**678,222**
Net investment gains or (losses)	134,342
Net Income (Loss)	**$ 812,564**

Capital and Surplus Account

Surplus as Regards to Policyholders, December 31, 2002	$ 2,510,991
Net Income or (Loss)	812,564
Change in non-admitted assets	(35,734)
Surplus as Regards to Policyholders, December 31, 2003	**$ 3,287,821**

Notes to the Financial Statements

-- None --

Examination Changes

-- None --

General Comments and/or Recommendations

Nurse Advice Agreement (page 11)

The Company should amend the Administrative Service Agreement for Nurse Advice Services so that it reflects the intentions of the parties.

Guaranty Agreement (page 12)

The Company is directed to file the Guaranty Agreement with the MDI as required by Section 382.195, RSMo (Transactions Within a Holding Company System). This requires a Form D filing in accordance with 20 CSR 200-11.101.

Asthma Grant Agreement (page 12)

The Company is directed to ensure that any future intercompany agreements of this type are filed with the MDI as required by Section 382.195, RSMo. In addition, the Company should ensure that such agreements are properly disclosed on it Insurance Holding Company System Annual Registration Statement.

Premium Deficiency Reserve (page 20)

The Company's management should ensure that the certifying actuary opines on the premium deficiency reserve in future opinions even if the premium deficiency reserve is determined to be zero.

Custodial Agreements (page 21)

The Company should amend or restate its custodial agreements so that they contain all of the NAIC safeguard provisions specified in Part 1, Section IV of the NAIC Financial Condition Examiners Handbook.

ACKNOWLEDGMENT

The assistance and cooperation extended by the officers and the employees of Family Health Partners, Inc. during the course of this examination is hereby acknowledged and appreciated. In addition to the undersigned, Barbara Bartlett, CPA, and Andy Balas, CFE, examiners for the Missouri Department of Insurance, participated in this examination. Karen Elsom, FSA, MAAA of Lewis and Ellis, Inc. also participated as a consulting actuary.

VERIFICATION

State of Missouri)
)
County of)

I, Mark A. Nance, on my oath swear that to the best of my knowledge and belief the above examination report is true and accurate and is comprised of only facts appearing upon the books, records or other documents of Family Health Partners, Inc., its agents or other persons examined or as ascertained from the testimony of its officers or agents or other persons examined concerning its affairs and such conclusions and recommendations as the examiners find reasonably warranted from the facts.

____
Mark A. Nance, CPA, CFE
Examiner-In-Charge
Missouri Department of Insurance

Sworn to and subscribed before me this _______day of ________, 2004.

My commission expires: ________________ __________________________
Notary Public

SUPERVISION

The examination process has been monitored and supervised by the undersigned. The examination report and supporting workpapers have been reviewed and approved. Compliance with NAIC procedures and guidelines as contained in the Financial Condition Examiners Handbook has been confirmed.

____
Frederick G. Heese, CPA, CFE
Audit Manager
Missouri Department of Insurance